GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Chief Financial Officer
Office of Tax and Revenue

Stephen M. Cordi
Deputy Chief Financial Officer

MEMORANDUM

TO: Robert Andary, Executive Director
Office of Integrity and Oversight

FROM: Stephen M. Cordi
Deputy Chief Financial Officer

DATE: September 30, 2009

SUBJECT: Internal Audit of the Refund Process

This is in response to your memorandum dated March 13, 2009, OIO's Results of our Review of OTR Refunds (IA:OTR:2807:M04).

1. Automated Refunds: Invalid Refunds Issued in Less than 10,000 Categories.

We concur with your findings and have implemented the following:

The Refund Control Unit (RCU) currently conducts a review of those refunds listed on the daily check register in which we select between 5 and 10 refunds under $10,000 to review to determine the validity of the refunds. The actual number of items under $10,000 reviewed by RCU depends upon the number of refunds that have to be reviewed on daily basis that are over $10,000.

2. Manual Refunds: Error noted in manual refunds issued.

We concur with your findings and have implemented the following:

As of January 2008, the Refund Control Unit (RCU) performed a 100% review of SOAR manual refunds regardless of the dollar amount.

3. The Refund Directive is still in Draft and Requires Additional Information

We concur with your findings and have implemented the following:

The Office of Tax and Revenue implemented the Interim Refund Directive in December 2007 in response to the breakdown in the internal controls related to the SOAR manual refund process. On May 15, 2009, the Office of Tax and Revenue finalized the Directive and launched a series of refund workshops to educate the OTR Directors and staff of the recent changes. Some of the noted changes consist of the following:

The SRRV (SOAR Refund Revenue Voucher) requires printed name and signature of the preparer, reviewer and approver.

The SOAR/ITS Refund Review Certification Form was revised to state that reviewers have ensured appropriate supporting documentation is included in the refund packages.

The SRRV and Refund Directive now contain guidance on the correct agency object codes to select for various tax refund types. Reviewers and approvers are also certifying that the agency object code selected is correct.

The Refund Directive contains additional SOAR manual refund categories and documentation requirements for refund types not included in the Interim Refund Directive.

4. Revenue Accounting Administration (RAA) does not follow-up on ITS and SOAR refund administration referrals

We concur with your findings and have implemented the following:

During FY 2008, the Refund Control Unit established a 2nd Notification process. The 2nd Notification follows-up with each administration for which RCU had previously referred a refund for correction that is still in pending status. The 2nd notification requests that the administration provide RCU with the status and expected resolution date of those refunds still pending within three days of receipt of the e-mail notification from RCU. These notifications are currently being sent on a quarterly basis.

RCU is currently updating all ITS refunds previously referred with notes (for those where no action has been taken to resolve the issue) and will ensure that notes are entered into ITS for any future refunds referred within 48 hours of sending out the referral. The 2nd Notification spreadsheet is also used to capture pertinent information such as amount refunded, average processing days, the dollar amount of refunds still pending, the total number of checks refunded and still pending, and the average number of days pending refunds are outstanding.

5. Other Matters

These items have been referred to Compliance for further action.

Thank you for the opportunity to respond to these findings. If you have any questions regarding this response, please contact Bert Molina, Director of Revenue Accounting, at 202-442-6451.

Cc: Lucille Dickinson, Chief of Staff, OCFO
Angell Jacobs, Director of Operations, OCFO
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GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Chief Financial Officer

Office of Integrity and Oversight



MEMORANDUM

TO: Stephen Cordi, Deputy Chief Financial Officer
Office of Tax and Revenue

FROM: Robert G. Andary, Executive Director
Office of Integrity and Oversight

DATE: March 13, 2009

SUBJECT: Results of our Review of OTR Refunds (IA:OTR:2807:M04)

The purpose of this memorandum is to present the results of our tests of the refunds issued by the Office of Tax and Revenue (OTR) throughout FY 2008. The Office of Integrity and Oversight (OIO) reviewed refunds on a test basis as part of our remediation of OTR's FY 2007 Material Weakness (Yellow Book) findings. The purpose of the review was to determine if the controls that were established as a result of the fraud were functioning as designed.

In the FY 2007 annual financial statement audit, BDO performed extensive work on OTR refunds as a result of the fraud of over $50 million through false refunds of Real Property Tax. BDO's audit identified several weaknesses in the processing of refunds, which OTR addressed throughout FY 2008.

In the FY 2008 annual financial statement audit, BDO conducted detailed audit work of OTR refunds issued in FY 2008, testing a large volume across tax types. The results of that audit were disclosed in the District's FY 2008 Yellow Book Report. BDO findings in FY 2008 were separated by Automated Refunds versus Manual Tax Refunds summarized as follows:

A. Automated Refunds

1. Unidentified Taxpayer Accounts and Converted Remittances in the Integrated Tax System (ITS).
2. Integrated Tax System (ITS) User Rights
3. Transfer and Adjustments to Taxpayer Accounts within ITS
4. Reconciliation between SOAR and the Integrated Tax System- Undelivered Tax Refund Checks
5. Real Property Tax Refunds Processed through the Integrated Tax System

6. Legible Scanned Copies of the Original Tax Return not maintained as supporting documentation.
7. Withholding payments processed through the integrated tax system
8. Voided or Canceled Checks processed through the integrated tax system

B. Manual Tax Refunds

1. Policies and Procedures for Processing a Manual Tax Refund
2. Internally Generated Standard Form for Requesting and Processing
3. Lack of Adequate Supporting Documentation
4. Refund Review Certification Form
5. Manual Refunds posted to the incorrect agency code

In our sample testing of refunds, we noted similar issues as stated by BDO in the FY 2008 Yellow Book Report. In addition, there were other items that came to our attention not included in the BDO comments and we include herein recommendations that should be considered by OTR as it continues to review and improve the refund process and related controls.

FINDINGS

1. Automated Refunds: Invalid Refunds Issued in Less than 10,000 Category

Under the new Interim Refund Directive, refunds less than $10,000 ***are not*** subject to the same multi-level tiered review as refunds greater than $10,000. As part of our review, we selected 105 refunds less than $10,000. Of the 105 returns reviewed totaling $78,538, we noted 5 of the 105 were invalid refunds totaling $7,205.89 or 9% of the total. The refunds were invalid for the following reasons:

Table 1: Invalid Reason

Error Reason	Item Count	Dollar Amount
OTR keying error	1	$3404.89
Minimum balance write off, taxpayer subsequently paid	3	71.00
Taxpayer misstated withholding on W-2	1	3730.00
Total	5	$7205.89

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In addition to the errors noted in Table 1, we found items that did not ultimately impact the validity of the refund; however, they impact the accuracy of data within ITS:

a. Address *errors on the taxpayer profile*

Of the 105 refunds reviewed, we found the following address errors:

Table 2: Address Errors in Taxpayer Profile

Error Reason	Item Count
Address apartment number truncation on profile (ELF returns)	5
OTR Keying Error	3
Taxpayer error (typing error)	2
Total	10

Prepared by OIO

b. *Taxpayer Name error*

We noted one incident where the taxpayer's first name was incorrectly keyed

c. *Missing image*
We could not view the image on line in two instances.

d. *W-2 errors.*

When a taxpayer filed electronically through e-file (ELF), we were able to verify the employer on the W-2 as an extra validation. Of the 52 ELF returns in our sample, we noted the following errors:

Table 3: W-2 Error in e-File

Error Reason	Item Count
Federal Employer EIN incorrectly reported in ITS (OTR Error)	3
Taxpayer error (typing error)	3
DC Government not in ITS*	1
Employer not found in ITS (see other matters)	1
Total	8

Prepared by OIO

*We noted that DC Government is not listed in ITS, due to the way the District reports withholding in the general ledger; therefore, this is not an error.

The validity of the ELF W-2 and withholding identification will have an impact as OTR goes forward with W-2 matching. Typographical errors may lead to incorrect matching results.

The majority of refunds issued by OTR to individuals are less than $10,000. Thus, the volume of refunds that are not subject to managerial review leaves OTR vulnerable to misappropriation and fraud.

Recommendation:

We recommend OTR incorporate a review of refunds less than $10,000 on a ***sample basis*** as part of its effort to safeguard the District's assets.

2. Manual Refunds: Errors noted in manual refunds issued

OIO selected 88 manual refunds, 48 greater than $10,000 and 40 less than $10,000. The following are the results of our test work:

In refunds greater than $10,000, we noted:

- 3 out of 48 refund vouchers totaling $70,653 did not have adequate supporting documentation attached, such as the tax sale registration and unsigned certificate of sale. This represents 6% of the sample population tested.

- 8 out of 48 refund vouchers totaling $445,153 included one refund totaling $324,674 that was not properly signed by the SOAR approver. This represents 17% of the sample population tested.

Of the 40 SOAR manual refunds less than $10,000 tested, we noted:

- 3 out of 40 refund vouchers totaling $14,142 did not have adequate supporting documentation attached, such as the ITS buyers report. One of the three refund vouchers lacked supporting documentation in the amount of $845 was handwritten.[1] This refund was issued prior to the issuance of the Refund Review Directive and was not authorized or certified by administration personnel, as prescribed by the Directive. This represents 7% of the sample population tested.

- 10 out of 40 refund vouchers totaling $59,025 were not properly signed by the SOAR approver. This represents 25% of the sample population tested.

It is the responsibility of each administration to properly prepare, review, approve, and attach related supporting documents to all refund vouchers before payment is processed. When this process is not followed, the refund should not be issued.

[1] In our final report on the Review of the Office of Tax and Revenue Tax Sale Program (Report No.: IA: OTR:2803-C04), we noted that the use of handwritten vouchers increases the risk of duplicate refunds to taxpayers. We were unable to determine the reason for the issuance of handwritten vouchers for redemption refunds.

Recommendation:

We recommend the refund threshold for manual refunds be decreased to $1,000 for all tax types. OTR staff should continue to work with the Information Systems Administration on automating refund processes.

3. **The Refund Directive is still in Draft and Requires Additional Information**

The Office of Tax and Revenue issued the interim refund directive in December 2007, as the immediate response to the breakdown in internal controls. The directive as of FY 2009 is still in draft status and is still not complete for all refund types. As noted by BDO, the supporting documentation requirements should be refined and updated regularly to ensure that all staff are aware of the requirements for a refund.

Recommendation:

We recommend OTR senior management update the Refund Directive and make it final. In addition, it should include examples of refund packages to provide employees with a reference point when preparing and reviewing a refund package. The package should also provide guidance on interest calculations in the case of manual refunds. Upon completion of the directive, it should be used as a training tool for all staff.

4. **Revenue Accounting Administration (RAA) does not follow-up on ITS and SOAR refund administration referrals**

We found that the RAA/Taxpayer Account Maintenance Unit (TAMU) did not properly track ITS and SOAR refund administration referrals that were outstanding, and had not been returned to RAA for approval and processing. We reviewed the ITS and SOAR refund referral logs during the period of June 2008 to September 2008. During this review, we noted 163 SOAR referrals with 50 cases still open and 173 ITS referrals all showing as open. RAA staff did not reflect the status of the case in the log.

RAA/TAMU may reject a refund that comes for approval. We noted that each refund was recorded in the Check Register Pending Referral Tracking Log and the SOAR Refund Tracking Log identified by voucher number, check register date/date received, administration, credit balance/amount, cause for referral, and referred for solution date/date approved. Referral conditions identified were:

- tax identification number discrepancies
- the property has not been redeemed
- clarification needed on the tax year
- voucher issued on killed property lot
- incorrect SSN
- refund to be processed in ITS rather than SOAR
- incorrect square/suffix/lot number
- missing documentation

- unauthorized signature approvals
- no signature forms attached
- no supporting documentation
- requires further review from audit

In reviewing the ITS Referral Tracking Log, we found that the log includes columns for "Potential Solution Per TAMU" and "Referred For Final Resolution Date," however there is no column indicating the date the administration resolved the issue and sent the refund back for approval or the date the refunds were cancelled.

In addition, we noted duplicates in the referral tracking sheet due to multiple referrals. We reviewed ten items within the June/July period and found that RAA denoted the pending status in the notes section of ITS; however, we found that 9 of the 10 were subsequently refunded. There was no note in ITS stating that the referral was resolved or how it was resolved, and there is no notation on the referral log to make it appear as an open case.

Without a mechanism to follow-up on the resolution of refund referrals, RAA is unable to determine the refund review closure rates and the types of errors that would assist with training staff and determining the effectiveness of the process.

Recommendation:

We recommend RAA establish a follow-up process to ensure timely approval of ITS and SOAR refunds and close out the case in the referral log so that management can measure closure rates and determine the time it takes to close cases. The status of cases should be referenced in the referral log. This will assist RAA in identifying issues with refunds, resolution time, and track performance by administration. With this type of data, TAMU can provide specific training to the areas on a timely basis. TAMU should immediately develop follow-up procedures and perform routine follow up communication with OTR administrations on refunds that have been referred back.

Other Matters

While we did not perform an audit of the tax returns identified in Table 4, items came to our attention that warrant further review by Compliance Operations Administration, as shown below:

Table 4

Entity ID	Transaction Number	Tax Year	Amount	Referral Reason
Taxpayer A	9100031627008	2007	1044.00	T/P files each year with MD address or Part-Year filer with MD address.
Taxpayer B	9100031729382	2007	1033.00	The taxpayer address does not exist per whitepages.com. Employer questionable.
Taxpayer C	9100028430263	2007	168.61	Taxpayer Schedule A, claimed income tax and general sales tax; however, you can only claim one or the other.

Completed by OIO

Recommendation:

We recommend OTR Compliance Operations Administration review these items to ensure that they are proper and valid.

As part of our continued monitoring efforts of the Office of Tax and Revenue, OIO will perform regular reviews of both manual and electronically issued refunds to ensure that controls remain in place and to suggest areas of improvement as OTR continues to work to improve controls over the process. We will contact the respective areas of OTR to obtain refund documentation and report issues that come to our attention on a routine basis.

If you have any questions regarding the issues noted in this memorandum, please contact Tisha Edwards, audit manager, at (202) 478-9143.

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